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No. 352

In the Supreme Court of the United States

OCTOBER TERM, 1930

V. LOEWERS GAMBRINUS BREWERY COMPANY,
PETITIONER

v.

CHARLES W. ANDERSON, INDIVIDUALLY AND AS COLLECTOR OF INTERNAL REVENUE OF THE UNITED STATES

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT

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OPINIONS BELOW

The District Court rendered no opinion but made findings of fact and conclusions of law (R. 22–26), which are not reported.

The opinion of the Circuit Court of Appeals (R. 212) is reported in 42 F. (2d) 216.

JURISDICTION

The judgment of the Circuit Court of Appeals reversing the judgment of the District Court for the Southern District of New York was entered on May 26, 1930. (R. 213.) Petition for a writ of

certiorari was filed August 16, 1930, and granted by this Court on October 20, 1930. (R. 214.)

The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Did Congress intend by Section 234 (a) (7) of the Revenue Act of 1918 to authorize a deduction for obsolescence of tangible property caused by the imminence of prohibition legislation?

2. The property which is the subject of the claimed deduction was used after the effective date of prohibition for the manufacture of near beer and other purposes. Since prohibition legislation placed no restriction upon the continued use of the property for these purposes, the question arises whether the deduction may, in any event, be allowed under the facts of this case.

STATUTE INVOLVED

Revenue Act of 1918, c. 18, 40 Stat. 1057, 1077, 1078:

> SEC. 234. (a) That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:
>
> * * * * *
>
> (7) A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence; * * *.

STATEMENT

This case reached the Circuit Court of Appeals on the appeal of the respondent, a Collector of Internal Revenue, from the judgment of the District Court in favor of the petitioner for refund of income and profits taxes for the years 1918 and 1919, in the aggregate amount of $22,091.20, together with interest and costs. (R. 209.) The District Court allowed deductions on account of obsolescence claimed by petitioner but disallowed by the Commissioner.

The District Court held that the petitioner was entitled to a deduction for each of these years, (1) for obsolescence of its brewery buildings and (2) for obsolescence of its good will, and that the deduction on account of each of these items was greater than the income computed without such deduction. (R. 26.) The Circuit Court of Appeals held that the law did not permit a deduction for either and reversed the judgment. (R. 212–213.) The order granting the writ of certiorari provides that "the arguments and briefs * * * be limited to the question whether the petitioner is entitled to any deduction for obsolescence of its tangible property in the taxable years 1918 and 1919 under Sec. 234 (a) (7) of the Revenue Act of 1918." (R. 214.)

Consequently only such of the facts and findings as relate to the deduction for obsolescence of the buildings, are here considered. The case was tried

on written waiver of jury trial by the District Court. Both parties presented requests for findings of fact. Those submitted by the petitioner [plaintiff] were adopted by the court in full. One or two of the findings submitted by the respondent were adopted with some changes. The respondent filed exceptions to most of the findings of fact made by the court and to the refusal of the court to adopt the findings of fact proposed by him. (R. 33–34.) The assignment of errors filed in the District Court raised the question of the sufficiency of the evidence to support the findings objected to. (R. 210, 211.) This matter was not reviewed by the Circuit Court of Appeals. (R. 212.) In view of our contention that, even if the statute does permit a deduction for obsolescence of the tangible property of a brewery caused by prohibition legislation, the facts here do not establish a basis for such a deduction, we discuss certain of the findings and in the argument refer to testimony upon which we rely.

The following matters are not disputed: Petitioner was and is a New York corporation, having its principal place of business in the City of New York. From 1879 until October 29, 1919, it was engaged in the manufacture and sale of lager beer, ale, and porter. On January 31, 1918, it had become a matter of common knowledge and was known to the petitioner that prohibition would take effect; and prohibition became effective on January 16, 1920. The buildings here involved were

constructed especially for the purpose of manufacturing, selling, and delivering beer, ale, and porter; and on January 31, 1918, they had a depreciated cost value of $153,932.18. In October, 1919, the petitioner discontinued the manufacture of intoxicating beverages. (R. 22–25.)

The District Court also made the following finding, suggested by the respondent but modified by the court, the correctness of which we do not dispute (R. 32):

> 22. That subsequent to Prohibition plaintiff to a small extent continued the manufacture of beers, ales and porter having an alcoholic content not in excess of one-half of one per cent and it still continues to manufacture such beverages to a small extent.

The District Court also made the following findings, the italicized portions of which we contend are inconsistent with the finding above quoted or are not supported by the testimony (R. 25):

> 14. That on the 31st day of January, 1918 it had become a matter of common knowledge and was known to the plaintiff that prohibition would become the law of the land and *that as a result of such law persons engaged in the business of manufacturing and selling beers, ales and porter including this plaintiff would suffer obsolescence in the value of their capital assets,* and such

prohibition became effective January 16, 1920.

15. That at January 31, 1918 the depreciated cost of buildings used by the plaintiff in its manufacturing operations as found by the Commissioner of Internal Revenue was the sum of $153,932.18. That *said buildings* were constructed especially for the purposes of manufacturing, selling and delivering beers, ales and porter and *were not commercially adaptable for any other use.*

That at January 16, 1920 such buildings had no salvage value.

15. That as a result of prohibition and beginning January 31, 1918 and ending January 16, 1920, the plaintiff suffered obsolescence of said buildings equal to the total depreciated cost thereof, to wit: $153,932.18 which should be ratably apportioned over such period.

ARGUMENT

We maintain that the Circuit Court of Appeals was correct in holding that Congress did not intend to provide compensation in any form for losses caused by prohibition legislation, and that, consequently, there can be no deduction for obsolescence in the instant case even upon the findings of the District Court. The arguments in support of this position are made on pp. 9–12 of the brief for petitioner in *Burnet, Commissioner,* v. *Niagara Falls*

Brewing Company et al., No. 61, October Term, 1930, to which reference is hereby made. Copies of that brief have been furnished to counsel for petitioner herein.

Even if this contention be overruled, we maintain that the judgment below should be affirmed on the ground that there was in fact no obsolescence of petitioner's property during 1918 or 1919. From its very nature, obsolescence begins only when there is a reasonable certainty that the property will become obsolete. (See pp. 13–14 of brief for the petitioner in *Burnet* v. *Niagara Falls Brewing Co.*, No. 61.)

Whether property is becoming obsolete is a question of fact. The burden was upon the taxpayer to show that it was entitled to the deduction which the Commissioner had disallowed and that the additional tax was to that extent illegally assessed. We challenge the findings of the District Court that on January 31, 1918, it was apparent that the petitioner "would suffer obsolescence in the value of their capital assets," and that the buildings in question were not "commercially adaptable for any other use" than "manufacturing, selling and delivering beers, ales and porter." (R. 25.) If these findings are susceptible of the meaning that on January 31, 1918, it was apparent that the buildings would, upon the advent of prohibition,

have no value, we maintain that they are not supported by the evidence.

No witness testified that before the advent of prohibition it was reasonably apparent that the buildings would have no value. The testimony showed that after the adoption of national prohibition the petitioner manufactured "near beer," using the same plant, or part of the same plant, and that this continued up to the time of the hearing in 1928. (R. 32, 67, 68, 70–71, 75–76, 84, 99, 101.) Although it does appear that the use of the plant for the manufacture of "near beer" has been very much less than it was for the manufacture of intoxicating beverages and that the present business is not nearly as profitable as the former (R. 70–72, 74, 77), it is not shown that this was foreseen during the years in question. Apparently the only reason why more of the buildings are not used in the manufacture of "near beer" is the lack of a sufficiently large volume of business. (R. 110, 115.) Moreover, parts of the buildings have been used for cold storage purposes (R. 74, 132–133) and other parts for the storage of theatrical scenery and electric cars. (R. 73, 100, 101, 131.)

In view of this testimony, we submit the findings are not warranted merely because of the testimony of building experts that the buildings "do not lend themselves economically to other purposes," and

that reconstruction would involve a prohibitive expense. (See R. 126, 134, 142.)

It does not appear that by the end of 1919 the petitioner regarded its buildings as worthless. Thereafter the petitioner received several inquiries and at least one offer for the purchase of the property. (R. 111, 120, 122–123, 125.) Apparently the petitioner continued to insure the buildings up to the time of the trial. (R. 162–166, 209.) There is testimony that the real estate of the petitioner would be more valuable without the buildings than with them, and that the buildings have no "salvage value." (R. 115.) This, we submit, is not equivalent to a finding that the buildings themselves had become valueless because of obsolescence in 1919. It often transpires that land without buildings is more valuable than land with the existing buildings on it, not because the buildings are obsolete, but because the land could be used for the erection of buildings which would produce far more income. There is uncontradicted testimony that the value of the real estate of the petitioner as a whole increased during the years 1918 and 1919. (R. 112.)

The argument of the respondent on this point is similar to that made on pp. 13–18 of the brief for the petitioner in *Burnet* v. *Niagara Falls Brewing Co.*, No. 61.

CONCLUSION

The judgment of the Circuit Court of Appeals should be affirmed.

Respectfully submitted.

THOMAS D. THACHER,
Solicitor General.
G. A. YOUNGQUIST,
Assistant Attorney General.
CLAUDE R. BRANCH,
SEWALL KEY,
J. LOUIS MONARCH,
JOHN MACC. HUDSON,
Special Assistants to the Attorney General.
PAUL D. MILLER,
Attorney.

C. M. CHAREST,
General Counsel,
Bureau of Internal Revenue.

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